Inflation Conundrum in Indian Economy

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Abstract

Economic growth with price stability had remained one of the uncontested objectives of economic planning in India. The problems India faces are challenging and the correctives required are bound to be complex and painful when vast changes in the global economic conditions as well as political-strategic alignments have taken place to aggravate its problems. The problem of price inflation attracted attention only after the Second World War. Rising prices were considered signs of good items and rising profits while failing prices were thought of as a sign of poor trade and poor profits. Inflation was regarded as a disease, caused by monetary mismanagement, which devastated business and the financial sector along with people's confidence in the currency. The objective of the paper is to assess the nature and pattern of inflation and its impact on performance of various sectors in Indian economy. The research work considers three important phases Such as : **First Phase:** Nationalisation of Reserve Bank of India (1949) to Nationalisation of Commercial banks (1969), **Second Phase:** Nationalisation of Commercial banks (1969) to before the introduction of New Economic Reforms (1991) and **Third Phase:** After the Introduction of New Economic Reforms (1991) to 2014. Further suggestions are also forwarded to abate and prevent inflationary pressure in India.

Keywords: Inflation spiral, GDP, WPI, CPI, GDP deflator and BRICS

Introduction

Economic growth with price stability had remained one of the uncontested objectives of economic planning in India. India entered the twenty first century in an extremely stretched position with economy and polity in grave imbalance and distortions. A sentimental or smug view is, no longer valid. The problems India faces are challenging and the correctives required are bound to be complex and painful when vast changes in the global economic conditions as well as political-strategic alignments have taken place to aggravate its problems (Shah, K.R.). The concept of inflation has undergone considerable modification since it was first treated by neo-classical economists. To them, inflation usually meant today's hyperinflation, or a complete loss of confidence in the currency, resulting in astronomical price rises and perhaps a total breakdown of the monetary system. It is generally observed that fluctuations in trade are accompanied by fluctuation in prices. More specifically, rising prices were considered signs of good items and rising profits while failing prices were thought of as a sign of poor trade and poor profits. These reflected movements, and adjustments were expected to take place in the normal business years. But inflation was regarded as a disease, caused by monetary mismanagement, which devastated business and the financial sector along with people's confidence in the currency.

The problem of price inflation attracted attention only after the Second World War. The neglect was due to the fact that the decade of the 1930's witnessed considerable price-stability. In the earlier periods, price had shown considerable cyclical swings, but no steady and secular upward movement. The objective of the paper is to assess the nature and pattern of inflation and its impact on performance of various sectors in Indian economy. Further suggestions are also forwarded to abate and prevent inflationary pressure in India (Amitabha De Santanu Bandyopadhyay).

Methodology Adopted

The research work considers three important phases for its analysis. The analysis data is divided into the following three vital stages of Indian economy. They are;

I. **First Phase:** Nationalisation of Reserve Bank of India (1949) to Nationalisation of Commercial banks (1969).

II. **Second Phase:** Nationalisation of Commercial banks (1969) to before the introduction of New Economic Reforms (1991)

III. **Third Phase:** After the Introduction of New Economic Reforms (1991) to 2014.

Measurement of Inflation

The IMF statistics highlighted those 24 countries in the world uses Wholesale Price Index (WPI) as an official measure to assess rate of inflation compared to 157 countries, which uses Consumer Price Index (CPI).

(i) Whole sale Price Index (WPI)

The WPI numbers reflect the changes in the general price level of a Country. For the WPI, basket of commodity is 676 is taken for measurement. Under this basket, there are three constituent commodity group found. They are;

a) Primary Articles (102)

b) Fuel, Power, Light and lubricants(19)

C) Manufactured Products (555)

With respective weights 20.118 percent, 14.910 and 64.972 percent respectively, WPI measures the changes in average prices of goods and services with companies the base year (2004-05) WPI (base year =100). If the current year WPI is greater than the base year index, it is called inflation (Kanagasabai, S).

(ii) Consumer Price Index (CPI)

It is also known as cost of living index number, are generally intended to represent the average change overtime in the prices paid by the ultimate consumer of a specified basket of goods and services. The CPI helps in determining the effect of rise and fall in prices of different class of consumers in different areas. The construction of such an index is of great importance because very often, the demand for higher wages is based on the cost of living index and wages and salaries in most countries are adjusted in tandem with CPI.

India launched CPI in January 2011. The CPI measures the prices of goods and services purchased by households. The data of CPI is collected from 310 cities and towns and 1,180 rural centers by NSSO and from selected villages by the Department of Posts. CPI measures retail prices in five major groups viz, food, clothing, housing, fuel and power. Food comprises the highest weighting of 45.50 percent in the CPI (Senthilkumar, P).

Inflation in BRICS Countries

The emerging countries in the world such as; Brazil, Russia, India, China and South Africa and its prevalence rate of inflation is given in Table 1.1.

Table 1.1 - Prevalence rate of Inflation among BRICS Economies

(in per cent)

Country	2010	2011	2014
Brazil	5.0	6.9	6.3
Russia	6.9	9.0	7.8
India	9.6	9.4	6.0
China	3.3	6.5	2.1
South Africa	4.3	5.0	6.1

*WPI for India and CPI for the other Countries (Deepak Mohanty)

Source: Inflation.eu World Wide Inflation Rate

It could be noted that the rate of inflation during 2010 and 2011 revealed a progressive tendency. The degressive rate of inflation is visualized only in India compared to other countries. It is an apparent observation that the rate of inflation is much higher in 2011 compared to 2010 and 2014. Among the countries, Russia and China has highest level of in inflation rate from 2010 to 2011. Among the economies, Russia has highest rate of inflation (7.8 per cent) in 2014.

Inflation in India

The prevalence rate of inflation in India since 1951 is classified into short term and long-term periods. The measurements of inflation including Wholesale Price Index (WPI), Consumer Price Index – Industrial Worker (CPI-IW) and Gross Domestic Product (GDP) of Indian economy is presented in Table 1.2.

Table 1.2 - Inflation in India: Medium to Long-term

(in per cent)

Period of Analysis	Decades	WPI	CPI-IW	GDP Deflator
Short term period	1949-50 to 1960-61	1.8	2.1	1.6
	1961-62 to 1970-71	6.2	6.5	6.2
	1971-72 to 1980-81	10.3	8.3	8.8
	1981-82 to 1990-91	7.1	9.0	8.7
	1991-92 to 2000-01	7.8	8.7	8.1
	2000-02 to 2010-11	5.4	5.2	5.1
	2011-12 to 2013-14	8.0	9.7	7.3
Long-term Period	**1949-50 to 2013-14**	**6.5**	**7.0**	**6.5**

Source: World Economic Outlook, (IMF) (Deepak Mohanty), 2014

With regard to WPI, India had experienced highest rate of inflation in 1971-1981, which account for 10.3 per cent. In the case of CPI-IW, it is highest during 1981-1991 (9.0 per cent). The GDP – deflator was again highest in 1971-1981, followed by 1981-1991 and 1991 to 2001. The average rate of WPI, CPI-IW and GDP deflator was 6.6, 7.1 and 6.5 per cent respectively for the whole period.

Impact of Inflation on Indian Economy

The onset of globalisation and opening of free market and trade between countries had made a sea change in the development of the country and the world at large. People have got lot of choices before making a decision on buying any products. The market has been flooded with global brands to the local brand. The per capita income and the purchasing power of the people have grown. The supply of money is plenty and at the same time, the value of money is coming down often because of inflation and devaluation of the currency. This trend is continuing of many years. The impact of inflation on selected variables of Indian economy is analysed and given in Table 1.3.

Table 1.3 - Impact of Inflation on the Performance of Indian Economy (1949-2014)

(in per cent)

SL. No	Variables	Years			Average Growth Rate
		1949-69	1969-91	1991-2014	
1	**Inflation**	**4.0**	**8.3**	**6,8**	**6.3**
2	GDP at factor cost	3.7	4.4	6.5	4.9
3	NDP at factor cost	3.8	4.3	6.3	4.8
4	GNP at factor cost	3.7	4.4	6.5	4.9
5	NNP at factor cost	3.7	4.3	6.3	4.8
6	Per capita NNP	1.6	2.0	4.6	2.7
7	Agriculture & Allied Activities at factor cost	37.30	40.87	5.12	27.8
8	Agriculture at factor cost	32.50	35.01	4.05	23.8
9	Food grain Production (in Billion)	79.9	129.8	210.5	140.1
10	Coffee Productions (in Million Tones)	NA	126.7	260.8	-
11	Tea Productions (in Million Tones)	NA	566.9	871.5	-
12	Oil seeds Productions (in Million Tones)	6.5	11.1	24.3	14.0
13	Sugarcane Production (in Million Tones)	83.9	165.2	292.3	180.5
14	Share of GDP Industrial Sector (in Billion)	17.30	16.38	15.4	16.4
15	SSI production (Rs. in Billion)	NA	898.3	5643.5	-
16	SSI Export (Rs. in Billion)	NA	27.4	1599.8	-
17	Service Sector Contribution GDP (in Per cent)	6.50	39.74	58.72	35.0

Source: Computed from Secondary Data
1949-69: Before Nationalisation of Banks
1969-91: After nationalization and before New Economic Reforms
1991-2014: After the Implementation of New Economic Reforms

The average growth rate of inflation for the 65 years of India accounts for 6.3 per cent. Among the three major phases, the rate of inflation was lowest during 1949-69. It is to state that after nationalization of banks and before the introduction of new economic reforms, the rate of inflation was highest during 1969-91. This increased rate of inflation was due to demand driven and supply shocks factors in India. The process of liberalization, privatisation and globalization has contained inflation at the modest of 6.8 per cent during 1991-2014. This is due to the inflow and outflow of goods and services and the paradigm shift in economic policies not only in India but also at the global level.

Since 1949, there is a positive growth visualized in all the variables. Among the three periods the rate of growth of economic variables found maximum in the economic reform period (1991-2014). The growth trajectory of Indian economy found convincing in 1991-2014 compared to other two periods ie. 1969 to1991and 1949 to1969.

Indian economy is structurally designed to rely on agriculture. It is evidenced from table 5.1 that the performance of industrial sector including SSI production and export level found insignificant over the years. It is witnessed that the service sector growth become transparent from nationalisation of the bank regime onwards is deduced from the analysis.

Inflationary Impact during Before and After Nationalisation in India

The inflationary impact on the select variables of Indian economy before and after nationalization is detailed in Table 1.4.

Table 1.4 - Impact of Inflation on the Performance of Indian Economy (1949-1991)

(in per cent)

SL. No	Variables	Periods		Variation	Average Growth Rate
		1949-69	1969-91		
1	**Inflation**	**4.0**	**8.3**	**4.4**	**6.1**
2	GDP at factor cost	3.7	4.4	0.7	4.05
3	NDP at factor cost	3.8	4.3	0.5	4.05
4	GNP at factor cost	3.7	4.4	0.7	4.05
5	NNP at factor cost	3.7	4.3	0.6	4.0
6	Per capita NNP	1.6	2.0	0.4	1.8
7	Agriculture & Allied Activities at factor cost	37.30	40.87	3.6	39.1
8	Agriculture at factor cost	32.50	35.01	2.5	33.7
9	Food grain Production (in Billion)	79.9	129.8	49.9	104.8
10	Coffee Productions (in Million Tones)	NA	126.7	NA	NA
11	Tea Productions (in Million Tones)	NA	566.9	NA	NA
12	Oil seeds Productions (in Million Tones)	6.5	11.1	4.6	8.8
13	Sugarcane Production (in Million Tones)	83.9	165.2	81.3	124.5
14	Share of GDP Industrial Sector (in Billion)	17.30	16.38	-0.9	16.8
15	SSI production (Rs. In Billion)	NA	898.3	NA	NA
16	SSI Export (Rs. In Billion)	NA	27.4	NA	NA
17	Service Sector Contribution GDP (in Per cent)	6.50	39.74	33.2	23.1

Source: Computed from Secondary Data
1949-69: Before Nationalisation of Banks
1969-91: After nationalization and before New Economic Reforms

The inflationary impact on Indian economy on the selected variables with regard to the two phases reflects vital economic findings of the Indian economy. The rate of inflation has grown from 3.9 to 8.3 per cent over the period (1949-69 to 1969-91). With regard to GDP at factor cost and NNP at factor cost reflects a slow growth rate in respect of before nationalization regime. The per capita NNP was also grown from 1.6 per cent to 2.0 per cent over the years.

The percent of variation in respect of agriculture and allied activities and agriculture sector gained momentum in the period. They account for 3.6 and 2.5 per cent growth during the years. The food grains production variation has triggered to the extent of 49.9 billion from 1949-69 to 1969-91 in India. It is also derived that coffee, tea, oil seeds and sugarcane production found progressive over the years. It is vivid to mention that the industrial sector share to India's GDP has achieved negative growth to the extent 0.8 to 0.9 per cent.

It is to highlight that inflation has positively impacted on Indian economy during 1949-69 and 1969-91 excepting the performance of industrial sector is derived from the analysis. The average growth of the selected variables conveyed a fact that food grains production and sugarcane production found maximum during the study period. Overall, the growth prospects in 1949-69 found very minimum compared to 1969-91, in India. The process of nationalization has delivered positive growth in every sector excepting industrial sector in India.

Inflationary Impact during Natioanalisation and Economic Reforms Regime in India

A comparative analysis between after nationalistion of banks and after introduction of New Economic Policy is detailed in the following table 1.5

Table 1.5 - Impact of Inflation on the Performance of Indian Economy (1969-2014)

(in per cent)

SL. No	Variables	Periods		Variation	Average Growth Rate
		1969-91	1991-2014		
1	**Inflation**	**8.3**	**6,8**	**-1.5**	**7.55**
2	GDP at factor cost	4.4	6.5	2.1	5.45
3	NDP at factor cost	4.3	6.3	2.0	5.30
4	GNP at factor cost	4.4	6.5	2.1	5.45
5	NNP at factor cost	4.3	6.3	2.0	5.30
6	Per capita NNP	2.0	4.6	2.6	3.30
7	Agriculture & Allied Activities at factor cost	40.87	5.12	-35.75	22.99
8	Agriculture at factor cost	35.01	4.05	30.96	19.53
9	Food grain Production (in Billion)	129.8	210.5	80.7	170.15
10	Coffee Production (in Million Tones)	126.7	260.8	134.1	193.75
11	Tea Productions (in Million Tones)	566.9	871.5	304.6	719.2
12	Oil seeds Production (in Million Tones)	11.1	24.3	13.2	17.70
13	Sugarcane Production (in Million Tones)	165.2	292.3	127.1	228.75
14	Share of GDP Industrial Sector (in Billion)	16.38	15.4	-0.98	15.89
15	SSI production (Rs. In Billion)	898.3	5643.5	4745.2	3270.90
16	SSI Export (Rs. In Billion)	27.4	1599.8	1572.4	813.60
17	Service Sector Contribution GDP (in Per cent)	39.74	58.72	18.98	49.23

Source: Computed from Secondary Data

1969-91: After nationalization and before New Economic Reforms

1991-2014: After the Implementation of New Economic Reforms

The two vital reforms period ie., after nationalization (1969-91) and after New Economic reforms (1991-2014) is studied through the comparative analysis of inflation with other selected other variables. The results of the study confirm that nationalsation of banks has created negative impact on inflation and positive impact on other variables in India. It could be noted that, the rate of inflation has decelerated from 1969-91 to 1991-2014 (ie., 8.3 per cent to 6.8 percent). The deceleration accounts to the total of -1.5 percent during the period. The process of nationalization has given a fill up to other selected variables over the years. The agriculture and service sector contribution to GDP also noticed some positive growth in Indian economy.

It is a fact that the increase in inflation has positively impacted on Small Scale Industries in India. The SSI production has increased from 898.3 billion to 5643.5 billion from the period 1969-1991 to 1991-2014. It is evidenced that the level of SSI exports also very positive over the years. Since the rate of inflation has come down, the economic variable has accelerated during the study period.

It could be explored that the reduction in the inflation rate (ie., from 8.3 per cent to 6.8 per cent) during the study period has given positive growth in the domain of food grains production, coffee production and tea production in India. The industrial sector contribution to GDP has come down (- 0.98 per cent) during the study period is evidenced from the study. It is therefore to state that the inflation control and reduction has reflected positive growth in many variables excepting the share of GDP by industrial sector.

Table 1.6 - Impact of Inflation on the Performance of Indian Economy (1949-2014)

(in per cent)

SL. No	Variables	Average Growth Rate		
		1949-69	1991-2014	Overall (1949-2014)
1	**Inflation**	**6.1**	**6.8**	**6.45**
2	GDP at factor cost	4.05	6.5	5.3
3	NDP at factor cost	4.05	6.3	5.2
4	GNP at factor cost	4.05	6.5	5.3
5	NNP at factor cost	4.0	6.3	5.15
6	Per capita NNP	1.8	4.6	3.2
7	Agriculture & Allied Activities at factor cost	39.1	5.12	22.1
8	Agriculture at factor cost	33.7	4.05	37.7
9	Food grain Production (in Billion)	104.8	210.5	315.3
10	Coffee Production (in Million Tones)	NA	260.8	NA
11	Tea Production (in Million Tones)	NA	871.5	NA
12	Oil seeds Production (in Million Tones)	8.8	24.3	16.5
13	Sugarcane Production (in Million Tones)	124.5	292.3	208.4
14	Share of GDP Industrial Sector (in Billion)	16.8	15.4	16.1
15	SSI production (Rs. In Billion)	NA	5643.5	NA
16	SSI Export (Rs. In Billion)	NA	1599.8	NA
17	Service Sector Contribution GDP (in Per cent)	23.1	58.72	51.8

Source: Computed from Secondary Data

1949-91: pre Reforms period

1991-2014: Post Reforms period

It is construed that the rate of inflation during the pre reform period was lower (6.1 per cent) compared to post economic reform period. In the post reform period, the rate of inflation was 6.8 per cent. It is due to the liberalized economic environment in India. In the closed economic regime, the rate of inflation was influenced largely by indigenous factors but in the case of post economic reforms period, it is influenced by exogenous factor also. The overall average rate of inflation for the Indian economy for 65 years accounts for 6.45 per cent. It is a fact that the GDP, NDP, NNP and Per capita NNP are growth significantly during 1991-2014 compared to 1949-1991.

With regard to agriculture and allied activities also found a significant growth during the post liberalization period. It is vital to highlight that the service sector contribution to India's GDP was highest during the open economic regime is found from the analysis.

Policy Implications

Inflation is a multi-dimensional and hydra-headed monster so that it needs a multi-pronged attack from all angles with synchronicity. Inflation in India is a structural as well as a monetary phenomenon. In the short term, localized demand – supply imbalances in wage goods, often due to seasonal variations in production coupled with market rigidities and regulatory failures have supported inflationary expectations that have resulted in a more widespread impact on the consumers. Monetary stability is imperative.

1. Supply side strategies for improving agriculture productivity, food market reforms throughout the supply chains and appropriate monetary and social policies are frequently needed to control inflationary pressure in India. Governments should be pro-active in this regard.

2. In India, public policy creation is inherently political and it is important that policy makers have access to the present sustainability trends to make better-informed policy decisions to achieve faster, more inclusive and sustainable growth in India.

3. Government of India and Reserve Bank of India need to examine the inflation challenges frequently and frame policies needed in the short run as well as longer run for accelerating Inclusive Growth and Development.

Conclusion

Indian economy is now a nearly two trillion-dollar economy. Recent estimates show that in terms of purchasing power parity, it is the third largest in the world, after USA and China. Inflation continues to be one of the major concerns from the perspective of its impact on economic growth and on the poor. The significant increase in prices tends to undermine the food security and livelihoods of the most vulnerable, by ending their already limited purchasing power. It is essential to consider the problem of inflation by Union Government, State Governments and Reserve Bank of India. There is an integrated efforts by every corner of planners and policy makers of India is required to combated inflationary pressure and to ensure long term growth trajectory viable to inclusive development

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